SUPREME COURT, U. S.

No. 73-618

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In the Supreme Court of the United States

OCTOBER TERM, 1973

HARRISON PROPERTY MANAGEMENT CO., INC., ET AL.,
PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

MEMORANDUM FOR THE UNITED STATES IN OPPOSITION

ROBERT H. BORK,
Solicitor General,
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1. On April 14, 1960, petitioners Walter J. Harrison, William H. Harrison and Lydia Harrison Couturie Ryan, dissolved a partnership and formed petitioner Harrison Property Management Co., Inc. ("Management"), a corporation to hold and manage 22,000 acres of land in Louisiana (the "Harrison Lands") for the development of income. The tract was adaptable to the trapping of fur-bearing animals and the production of oil and gas. The individual petitioners were the sole stockholders of Management. They transferred the Harrison Lands to Management on the date of its incorporation in fee without a warranty, but with full subrogation in and to all rights of warranty held by preceding owners and vendors (Pet. App. B 49-53).

Management opened a bank account and maintained books and records showing its receipts and disbursements.

In addition, it paid local taxes and instituted and defended suits involving the lands owned by it. During the years in suit (1960-1963), it held ten meetings of its board of directors and the minutes reflect authorization by the board for approval of six leases for mineral rights and several rights-of-way, which were all negotiated by the corporate officers. The board also approved a waiver of salaries for corporate officers, authorized a suit to confirm title to certain land, and authorized execution of a consent decree to extend the statute of limitations on the corporation's tax returns (Pet. App. B 57-59).

Contemporaneously with the incorporation, petitioners and Management entered into an agreement which recited that the transfer of property to the corporation was made "solely and only as a matter of convenience and accommodation and without consideration whatsoever" having been paid by Management, which disclaimed "any right, title, or interest" in and to the property other than the right to manage and administer it. Under the agreement, Management's expenses were to be charged against the three petitioner-shareholders in equal amounts by means of deductions from the proceeds of operations which were distributed periodically to the shareholders (Pet. App. B 40, 53-57).

For the period ending December 31, 1960, Management filed a fiduciary income tax return, showing its net income distributed on an equally proportionate basis to the three petitioner-shareholders. For each of the calendar years 1961, 1962 and 1963, Management filed corporate income tax returns, which reported no income or expenses but included schedules which showed all expenses paid by the shareholders reported on their individual income tax returns and showed the income and expenses allocated to them on the returns filed by Management (Pet. App. B 60).

On audit, the Commissioner of Internal Revenue determined deficiencies against Management on the ground that it was a taxable entity reponsible for reporting income from lands belonging to and managed by it. In a refund suit in the Court of Claims, the Trial Commissioner upheld the claimed refund (Pet. App. A 14-37). The Court of Claims, however, agreed that Management was a taxable entity and dismissed the petition (Pet. App. B 38-63).

2. In concluding that the income from the Harrison Lands was taxable to Management and not to its shareholders, the Court of Claims correctly followed the decisions of this Court in *Moline Properties* v. *Commissioner,* 319 U.S. 436 and *National Carbide Corp.* v. *Commissioner,* 336 U.S. 422. Those cases established the rule that a corporate entity cannot be ignored for federal income tax purposes as long as it is formed for business purposes or engages in business activity. Here, Management performed numerous functions in its own name which were more than sufficient to constitute business activity under *Moline Properties.*[1]

Urging that the status of Management was that of an agent, petitioners assert (Pet. 7-9) a conflict with

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[1] The Court of Claims stated (Pet. App. B 43), that the corporation—

> authorized and executed leases for mineral rights, granted several rights-of-way, sold some produce, acted as a party in litigation, hired executive officers, paid local taxes, maintained its building, kept a checking account, recorded its receipts and disbursements, held meetings of stockholders and directors, and followed the formalities of corporate operation. It was by no means dormant or inert. * * * We know of no case which, on similar facts, has disregarded the corporation, at the instance of the shareholders, as not engaging in enough business activity. * * *

National Carbide Corp. v. *Commissioner, supra.* They rely upon the statement in that case that "What we have said does not foreclose a true corporate agent or trustee from handling the property and income of its owner-principal without being taxable therefor." (336 U.S. at 437). But petitioners cannot avoid the impact of the Court's further statement (*ibid.*) that "If the corporation is a true agent, its relations with its principal must not be dependent upon the fact that it is owned by the principal, if such is the case. Its business purpose must be the carrying on of the normal duties of an agent."

Management, however, could not be characterized as carrying on the normal duties of an agent. As the Court of Claims found (Pet. App. B 45), Management was created solely to serve the beneficial owners of the property, who continued to control every aspect of its activities. It served no one else. Cf. *Carver* v. *United States,* 412 F. 2d 233 (Ct. Cl.). As a result, Management's relations with the beneficial owners were wholly dependent on the fact that they were its sole shareholders and did not involve their capacity as principals.[2] Under the standards of *National Carbide,* Management was not a "true agent" and must therefore be treated as a taxable entity required to report the income from its property.

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[2] Petitioners argue (Pet. 9-11) that the Court of Claims placed undue emphasis upon the fact that the beneficial owners of the property were the shareholders of Management. In their view, the recitations in the corporate charter that Management was organized to manage the property of "any person or persons * * *" should control. But, as the Court of Claims correctly stated (Pet. App. B 43, 46), the controlling tests to be applied here do not depend upon such semantic descriptions used by the parties to characterize their activities, but instead depend upon "the reasons why the 'dummy' was created, and what it actually does."

For the reasons stated, it is respectfully submitted that the petition for a writ of certiorari be denied.

ROBERT H. BORK,
Solicitor General.

NOVEMBER 1973.